

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

[Third Party Communication:

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:TEGE:EOEG:E0

PLR-134411-11

Date:

February 02, 2012

State =
Trust =

System =

Date 1 =
Date 2 =
Statute =

Agreement =
Employees =

Profession =

Dear

This letter responds to a letter from your authorized representatives dated August 5, 2011, in addition to supplemental information, submitted on behalf of Trust requesting a ruling that Trust's income is excludable from gross income under section 115 of the Internal Revenue Code. The Trust represents the facts as follows:

Facts

System established under State law became operational on Date 1. It is an actuarial, reserve joint-contributory retirement system for certain specified employees in Profession within State. Membership in System is mandatory for those specified employees of State in Profession. System's administration is the responsibility of the Board of Trustees. The Trustees and the Trust Administrator (selected by the Trustees) exert significant influence and control over System.

Trust Fund was created and established pursuant to Statute and adopted by System's Board of Trustees on Date 2. The Board of Trustees of System serves as the Board of Trustees of the Trust. The Board has arranged to provide Hospital and Medical Benefits for Retired Employees, Spouses and specified beneficiaries. The trustees may maintain separate sub-trusts or accounts in Trust Fund for appropriate categories of Eligible Recipients and Employers. The Board of Trustees amended Trust Agreement to provide that only contributions to Trust from State, political subdivisions of State and organizations whose income is excluded from gross income under section 115 will be credited to Trust.

The purpose of Trust Fund is to prefund costs for Hospital and Medical Benefits to retirees and eligible beneficiaries. Contributions to Trust Fund will be solely used to fund Employer's expenses for the post-retirement Hospital and Medical Benefits. The pre-funding is to satisfy the requirements of Governmental Accounting Standards Board (GASB) issued Statement No. 45 which requires accounting for post-employment health care benefits on an actuarial basis rather than on a pay-as-you-go basis.

In no event will Trust Fund assets be distributed to or revert to any entity that is not State, a political subdivision of State, or an entity whose income is excluded from gross under section 115 other than payments to retired employees and specified beneficiaries and for administrative expenses of Trust Fund.

Law and Analysis

Section 115(1) of the Code provides that gross income does not include income derived from any public utility or the exercise of any essential government function and accruing to a state or any political subdivision thereof.

In Rev. Rul. 77-261, 1977-2 C.B. 45, income from an investment fund, established under a written declaration of trust by a state, for the temporary investment of cash balances of the state and its participating political subdivisions, was excludable from gross income for federal income tax purposes under § 115(1). The ruling indicated that the statutory exclusion was intended to extend not to the income of a state or municipality resulting from its own participation in activities, but rather to the income of a corporation or other entity engaged in the operation of a public utility or the performance

of some governmental function that accrued to either a state or municipality. The ruling points out that it may be assumed that Congress did not desire in any way to restrict a state's participation in enterprises that might be useful in carrying out projects that are desirable from the standpoint of a state government and which are within the ambit of a sovereign to properly conduct. In addition, pursuant to § 6012(a)(2) and the underlying regulations, the investment fund, being classified as a corporation that is subject to taxation under subtitle A of the Code, was required to file a federal income tax return each year.

In Rev. Rul. 90-74, 1990-2 C.B. 34, the Service determined that the income of an organization formed, funded, and operated by political subdivisions to pool various risks (casualty, public liability, workers' compensation, and employees' health) is excludable from gross income under § 115 of the Code. In Rev. Rul. 90-74, private interests neither materially participate in the organization nor benefit more than incidentally from the organization.

Trust was organized pursuant to Statute by System to enable the pre-funding of health benefits for retired employees, their spouses and eligible dependents. Payment of such benefits constitutes the performance of essential government functions. Based upon Rev. Rul. 90-74 and Rev. Rul. 77-261, Trust performs an essential governmental function within the meaning of § 115(1) of the Code.

Trust income accrues to the State or political subdivisions of the State. No private interests participate in or benefit from the operation of Trust. Any distribution of funds in Trust can only be used to pay benefits, or revert to an entity, which is the State, a political subdivision or an entity whose income is excluded from income tax under section 115. The benefit to the participating employees is incidental to the public benefit. See Rev. Rul. 90-74.

Based on the information and representations submitted by Trust, we hold that the income of Trust is derived from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof for purposes of § 115(1). Accordingly, Trust's income is excludable from gross income under § 115(1) of the Code.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no representation is made that contributions or premiums paid on behalf of or benefits received by employees, former employees, retirees, spouses, dependents or others will be tax-free. This ruling concerns only the Federal tax treatment of Trust's income and may not be cited or relied upon as to any matter relating to the taxation of accident or health contributions or benefits.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Sylvia F. Hunt
Assistant Branch Chief
Exempt Organizations Branch
Office of Division Counsel /
Associate Chief Counsel
(Tax Exempt & Government Entities)

Enclosure: copy for ' 6110 purposes